

Message Text

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DODE-00 EB-07 FRB-01 H-02 INR-07 INT-05 L-03
LAB-04 NSAE-00 NSC-05 PA-02 EPG-02 AID-05 SS-15
STR-04 ITC-01 PRS-01 SP-02 FEAE-00 OMB-01 XMB-04
OPIC-06 /124 W

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O R 221613Z JUN 77
FM AMEMBASSY LONDON
TO SECSTATE WASHDC IMMEDIATE 5402
TREASURY DEPT WASHDC IMMEDIATE
INFO AMEMBASSY BONN
AMEMBASSY BRUSSELS
AMEMBASSY DUBLIN
AMEMBASSY NEW DELHI
AMEMBASSY PARIS
AMEMBASSY ROME
AMEMBASSY TOKYO
AMCONSUL BELFAST
AMCONSUL EDINBURGH
USMISSION GENEVA
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USEEC ALSO FOR EMBASSY
USOECN ALSO FOR EMBASSY
USMTN

DEPARTMENT PASS FEDERAL RESERVE BOARD

TREASURY FOR DONALD E. SYVRUD, OASIA

E.O. 11652: N/A
TAGS: ECON, UK
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SUBJECT: ECONOMIC DEVELOPMENTS FOR PERIOD JUNE 16 - 22

SUMMARY: THE ECONOMY CONTINUES TO OPERATE AT THE LEVEL
ESTABLISHED AT THE END OF 1976. INDUSTRIAL PRODUCTION
HASCHANGED ONLY marginally SINCE THEN.

AVERAGE EARNINGS DECLINED IN APRIL MAKING IT MORE
LIKELY THAT THE RISE THROUGH JULY WILL REMAIN WITHIN THE

SINGLE DIGIT GOVERNMENT TARGET. RETAIL PRICES ROSE MORE SLOWLY IN MAY. CUTTING THE 12-MONTH RATE OF PRICE INCREASE TO 17.1 PERCENT. HOWEVER, IN JUNE, UNEMPLOYMENT ROSE TO A POST-WAR RECORD AFTER 9 MONTHS OF VERY LITTLE CHANGE. THE APRIL CURRENT ACCOUNT SURPLUS EVAPORATED IN MAY BUT THE DEPARTMENT OF TRADE FORECASTS THAT EXPORT VOLUME FOR 1977 WILL BE 7 PERCENT ABOVE 1976'S LEVELS. BRITISH NATIONAL OIL CORP. RAISED \$825 MILLION IN ITS OWN NAME. THE BANK OF ENGLAND QUARTERLY DISCUSSES INDUSTRIAL PROFITABILITY AND MONETARY GROWTH TARGETS IN THE U.K. GILT PRICES EASED, BUT THE VARIABLE INTEREST ISSUE WAS EXHAUSTED. GDP ROSE SLIGHTLY IN THE FIRST QUARTER OF 1977. END SUMMARY.

1. RETAIL PRICES. THE RATE OF INCREASE IN RETAIL PRICES SLOWED IN MAY. AFTER RISING 2.6 PERCENT IN APRIL. THE INDEX OF RETAIL PRICES (RPI) (JANUARY 1974 EQUALS 100) ROSE 0.8 PERCENT IN MAY TO 181.7. THE SLOWING STEMMED LARGELY FROM A DECLINE IN SEASONAL FOOD PRICES COUPLED WITH THE 1 PERCENTAGE POINT DECLINE IN HOME MORTGAGE INTEREST RATES WHICH TOOK EFFECT IN MAY. IF SEASONAL FOOD PRICES (DOWN 4.6 PERCENT) ARE EXCLUDED THE RPI ROSE 1.0 PERCENT IN MAY. SINCE MAY 1976, RETAIL PRICES HAVE RISEN BY 17.1 PERCENT; HOWEVER. THE ANNUALIZED RATE OF 19.2 PERCENT OVER THE LAST 6 MONTHS REFLECTS THE MORE RAPID RATE OF PRICE INCREASE IN RECENT MONTHS.

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2. AVERAGE EARNINGS. PRETAX AVERAGE EARNINGS DECLINED IN APRIL. THE INDEX OF AVERAGE EARNINGS (JANUARY 1970 EQUALS 100) FELL 0.4 PERCENT TO 282.8 IN APRIL FROM 283.9 IN MARCH. THIS DECLINE INCREASES THE PROBABILITY THAT THE INCREASE IN AVERAGE EARNINGS DURING THE SECOND YEAR OF PAY RESTRAINT WILL REMAIN WITHIN THE GOVERNMENT'S (REVISED) SINGLE DIGIT TARGET. IN THE 9 MONTHS SINCE THE AUGUST 1, 1976 BEGINNING OF THE SECOND YEAR OF PAY RESTRAINT, AVERAGE EARNINGS HAVE RISEN BY 7.5 PERCENT. THE APRIL DECLINE IN EARNINGS WAS OFFICIALLY ATTRIBUTED TO REDUCED OVERTIME WORKING AND TO ABSENCE OF ANY SEASONAL BONUS PAYMENTS OF THE KIND WHICH CONTRIBUTED TO THE 1.8 PERCENT MARCH RISE. TAKING INTO ACCOUNT THE 2.6 PERCENT RISE IN RETAIL PRICES IN APRIL, REAL PRETAX AVERAGE EARNINGS HAVE DECLINED BY 6.8 PERCENT SINCE LAST AUGUST. WHILE PLANNED INCOME TAX REDUCTIONS WILL PROVIDE SOME RELIEF DURING THE SECOND HALF OF 1977, THE SEVERITY OF THE DROP IN REAL PRETAX EARNINGS DOES MUCH TO EXPLAIN THE SHARP DECLINE IN RETAIL SALES VOLUME WHICH BEGAN IN JANUARY. IT ALSO HELPS TO UNDERSTAND THE INCREASINGLY LOUD DEMANDS FROM MANY TRADE UNION LEADERS FOR A MORE

FLEXIBLE INCOMES POLICY. THE IMMEDIATE OUTLOOK FOR REAL EARNINGS IS NOT ROSY. RETAIL PRICE INCREASES SHOULD CONTINUE TO EXCEED RISES IN AVERAGE EARNINGS FOR SEVERAL MONTHS BY WHICH TIME THE INFLUENCES OF SLUGGISH DEMAND AND A STABLE EXCHANGE RATE SHOULD EXERCISE A MODERATING EFFECT.

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3. INDUSTRIAL PRODUCTION. INDUSTRIAL PRODUCTION WAS VIRTUALLY UNCHANGED IN APRIL, FROM A MARCH FIGURE WHICH WAS REVISED DOWNWARD BY 1.2 PERCENT. THE OVERALL INDEX OF INDUSTRIAL PRODUCTION (1970 EQUALS 100) FOR APRIL WAS

103.2 COMPARED WITH THE REVISED MARCH FIGURE OF 103.1.
THE NARROWER INDEX OF MANUFACTURING PRODUCTION DECLINED
BY 0.8 PERCENT TO 104.7 FROM A REVISED 105.5 IN MARCH.
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IN LIGHT OF THESE REVISIONS, INDUSTRIAL PRODUCTION WAS
STATIC BETWEEN THE FOURTH QUARTER OF 1976 AND THE FIRST
QUARTER OF 1977, WHILE MANUFACTURING OUTPUT ROSE BY A
SCANT 0.9 PERCENT. IN THE YEAR TO APRIL, THESE INDICES
ROSE BY 0.9 AND 1.4 PERCENT, RESPECTIVELY. DISAGGREGAT-
ING THE APRIL FIGURES REVEALS DECLINES IN THE OUTPUT OF
"FOOD' DRINK AND TOBACCO" (MINUS 1.8 PERCENT), "CHEMICALS,
WOOD AND PETROLEUM PRODUCTS" (MINUS 3.8 PERCENT), TEX-
TILES (MINUS 1.9 PERCENT) AND OTHER MANUFACTURING (MINUS
2.8 PERCENT). WITH ENGINEERING OUTPUT STATIC, SLIGHT
RISES IN METAL MANUFACTURING, MINING, QUARRYING AND "GAS,
ELECTRICITY AND WATER" WERE NOT ENOUGH TO PRODUCE MORE
THAN A MARGINAL INCREASE IN THE OVERALL INDEX. ON A MAR-
KET SECTOR PRICBASIS, THE OUTPUT OF CONSUMER AND INTER-
MEDIATE GOODS INDUSTRIES WAS STAGNANT IN APRIL WHILE IN-
VESTMENT GOODS OUTPUT DECLINED BY 1.0 PERCENT.

THE DEPARTMENT OF INDUSTRY BELIEVES THAT DESPITE THE
FLATNESS OF RECENT MONTHLY FIGURES, THERE WAS A SLOW RISE
IN THE UNDERLYING LEVEL OF INDUSTRIAL OUTPUT. THIS CON-
CLUSION IS BASED ON THE USE OF A DELIVERY RATHER THAN A
PRODUCTION-BASED INDEX IN MEASURING INDUSTRIAL OUTPUT.
THIS IS ESTIMATED TO HAVE IMPARTED A DOWNWARD BIAS OF
0.5 PERCENT TO THE INDEX IN BOTH THE FOURTH QUARTER OF
1976 AND THE FIRST QUARTER OF 1977. DESPITE THIS CAVEAT,
THE REVISION OF THE MARCH INDEX VIRTUALLY ELIMINATES THE
QUARTER-TO-QUARTER GROWTH ON WHICH THE INITIAL 0.5 PER-
CENT GROWTH IN OUTPUT-BASED GROSS DOMESTIC PRODUCT WAS
BASED.

4. UNEMPLOYMENT. UNEMPLOYMENT ROSE SHARPLY TO A POST-
WAR RECORD IN THE MONTH TO MID JUNE. ON A SEASONALLY AD-
JUSTED BASIS, 36,900 PEOPLE JOINED THE JOBLESS ROLLS
BRINGING THE TOTAL NUMBER OF UNEMPLOYED EXCLUSIVE OF
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SCHOOL LEAVERS TO 1.3528 MILLION (5.7 PERCENT). THE MORE
DRAMATIC INCREASE OF 108,364 IN THE UNADJUSTED FIGURES
WAS NEARLY ALL DUE TO THE ADDITIONAL 104,000 SCHOOL LEAV-
ERS WHO WERE LOOKINGFOR WORK.THEY INCREASED THE TOTAL UN-
EMPLOYED TO 1.4501 MILLION (6.2 PERCENT) FROM THE PRE-
VIOUS MONTH'S 1.3417 MILLION (5.7 PERCENT). THE JUNE IN-

CREASE. THE LARGEST MONTHLY CHANGE SINCE JULY 1976. MARKS AN ABRUPT CHANGE FROM THE VIRTUALLY STATIC FIGURES OF THE JANUARY-MAY PERIOD. THE DEPARTMENT OF EMPLOYMENT (DOE) HAS TAKEN THE VIEW THAT ONE MONTH'S DATA DOES NOT ESTABLISH A TREND. IT ALSO ADDS THAT A NEW AND MORE ACCURATE COMPUTERIZED SYSTEM FOR GATHERING DATA ON EXECUTIVE AND PROFESSIONAL JOBLESS MAY HAVE ADDED 5,000 TO THE MID-JUNE FIGURE. A DOE PRESS SPOKESMAN OPINED THAT THE JUNE 9 SURVEY DATE, FALLING DURING THE JUBILEE CELEBRATION, MAY HAVE CAUGHT EMPLOYERS DURING A WEEK WHEN THEY WERE MORE PRONE TO LAY OFF EMPLOYEES. WHATEVER THE EXPLANATION, THE CHANCELLOR'S NEGOTIATIONS WITH THE TRADE UNION LEADERSHIP ON PAY RESTRAINT WILL BE MORE DIFFICULT IN THE WAKE OF THE LATEST FIGURES.

5. CURRENT ACCOUNT. A 91 MILLION POUND INCREASE IN THE PETROLEUM TRADE BALANCE WAS LARGELY RESPONSIBLE FOR SHIFTING THE U.K.'S ESTIMATED CURRENT ACCOUNT FOR MAY BACK INTO A MARGINAL DEFICIT. (SEE LONDON 9984.)

6. THE DEPARTMENT OF TRADE, FOR THE FIRST TIME' USED A SURVEY OF THE U.K.'S 65 LARGEST EXPORTERS TO FORECAST TOTAL U.K. EXPORTS FOR 1977. EXPORT VOLUME IS EXPECTED TO BE FROM 3 TO 4 PERCENT HIGHER IN THE SECOND THAN IN THE FIRST HALF OF 1977. THE VOLUME FOR 1977 AS A WHOLE IS EXPECTED TO BE 7 PERCENT ABOVE THE 1976 LEVEL.

7. THE BRITISH NATIONAL OIL CORPORATION HAS RAISED \$825 MILLION IN AN UNSECURED LOAN. WITHOUT HMTREASURY GUARANTEE FROM A GROUP OF AMERICAN AND BRITISH BANKS. (THE NE-UNCLASSIFIED

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GOTIATION FOR WHICH IS REPORTED IN LONDON 9087.) \$675 MILLION OF THE LOAN ARE IN DOLLARS BEARING AN INTEREST RATE OF 113 PERCENT OF CITIBANK'S PRIME RATE FOR THE FIRST TWO YEARS AND 115 PERCENT OF ITS PRIME RATE FOR THE SECOND TWO YEARS. THE \$150 MILLION BALANCE WAS RAISED IN

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XMB-04 /124 W
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O R 221613Z JUN 77
FM AMEMBASSY LONDON
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EURODOLLARS WITH AN INTEREST RATE OF 1 PERCENT OVER THE
LONDON INTERBANK OFFER RATE FOR THE FIRST FOUR YEARS.
THE INTEREST RATE ON BOTH LOANS WILL RISE FURTHER AFTER
THE FIRST FOUR YEARS. THE STATE-OWNED FIRM FORMED 18
MONTHS AGO, HAS HERETOFORE BORROWED ONLY FROM OFFICIAL
SOURCES. THESE STATE BORROWINGS INCLUDE 186 MILLION
POUNDS AT 13.32 PERCENT AND 142 MILLION AT 14.14 PERCENT.

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8. THE BANK OF ENGLAND'S LATEST QUARTERLY BULLETIN
STRESSES THE NEED TO IMPROVE PROFITABILITY IN U.K. INDUS-
TRY. IT ALSO DISCUSSES AT LENGTH ITS VIEW OF MONETARY
TARGETS AND CONTROLS, MINIMIZING POSSIBLE ADVERSE EFFECTS
OF THE TIGHT MONETARY POLICY CARRIED OUT DURING THE LAST
SIX MONTHS. (SEE LONDON 10193.)

9. PRICES IN THE BRITISH FUNDS MARKET CONTINUED EASIER
OVER THE WEEK AS REDEMPTION YIELDS ON SOME LONG ISSUES
SURPASSED 13-1/2 PERCENT. MARKET SOURCES INDICATE THAT

THE INSTITUTIONS WHICH ARE NORMALLY HEAVY BUYERS HAVE BEEN RESTRAINED BECAUSE INTE- A LIA THE BP SALES AND THE FUNDS EARMARKED TO SETTLE INSTALLMENT PAYMENTS FOR THE PARTIALLY PAID GILTS HAVE TIGHTENED THEIR LIQUID POSITIONS.

ON WEDNESDAY MORNING, HOWEVER, A SHORT-LIVED SURGE IN THE MARKET EXHAUSTED THE VARIABLE RATE TREASURY 198L. 400 MILLION POUNDS OF THIS GILT WERE ISSUED AS A TAP STOCK ON MAY 30, 1977. AND IT HAS ENJOYED A GOOD MARKET RECEPTION. A SECOND TAP STOCK. THE TREASURY 11-3/4 PERCENT 1991, ISSUED ON JUNE 3, SHORTLY AFTER THE VARIABLE RATE GILT. ON THE OTHER HAND, HAS NOT SOLD WELL. 800 MILLION POUNDS OF THE 11-3/4 PERCENT BOND WERE PLACED ON THE MARKET AT A YIELD WHICH BECAME RAPIDLY UNATTRACTIVE AS GILT PRICES FELL. IT CURRENTLY YIELDS 12.83 PERCENT TO REDEMPTION.

10. DAVID HOWELL, CONSERVATIVE SPOKESMAN ON TREASURY AFFAIRS, CALLED FOR LESS EMPHASIS UPON LARGE-SCALE MANUFACTURING IN ECONOMIC PLANNING AND GREATER RECOGNITION OF THE EFFICIENCY OF SMALLER UNITS OF ENTERPRISE. (SEE LONDON A-43L.)

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11. BUSINESS ECONOMISTS FORECAST A MARGINAL INCREASE IN GDP THIS YEAR. (SEE LONDON A-430.)

12. STERLING HAD ANOTHER GOOD WEEK. MARKET SOURCES SPECULATE THAT THE BANK OF ENGLAND TOOK IN MODEST AMOUNTS LAST WEEK. MOST ACTIVITY REMAINS COMMERCIAL, WITH THE RATE PRIMARILY REFLECTING COMMERCIAL SUPPLY AND DEMAND CONSIDERATIONS. GOOD RETAIL PRICE AND MONETARY AGGREGATE STATISTICS HAVE GIVEN CONFIDENCE TO THE MARKET IN THE SHORT TERM. THE MAJOR NEGATIVE FACTOR REMAINS THE UNCERTAIN OUTLOOK FOR THE THIRD PHASE OF INCOMES POLICY. MARKET SOURCES BELIEVE THAT U.K. RESERVES IN JUNE AND JULY WILL SHOW LARGE INCREASES AS A RESULT OF THE BNOC ISSUE AND THE U.S. SALE OF BP SHARES.

13. GDP. PRELIMINARY EXPENDITURE DATA INDICATE THAT REAL GDP DECLINED BY 1.0 PERCENT DURING THE FIRST QUARTER OF 1977. THE INCOME AND OUTPUT-BASED INDICES SHOWED SMALL RISES (0.9 AND 0.7 PERCENT RESPECTIVELY) WITH THE RESULTANT AVERAGE ESTIMATE SHOWING A RISE OF 0.2 PERCENT OVER THE FOURTH QUARTER. THE EXPENDITURE DATA REVEALS A DISTURBING 4.3 PERCENT DECLINE IN GROSS DOMESTIC CAPITAL FORMATION. THIS MEANS THAT FIRST QUARTER FIXED INVESTMENT WAS 7.1 PERCENT BELOW THAT AVERAGE QUARTERLY LEVEL FOR 1976. OTHER NOTABLE FEATURES INCLUDE THE SHARPEST RISE

IN INVENTORIES SINCE THE THIRD QUARTER OF 1974 (345 MILLION POUNDS VS 86 MILLION IN 1976-IV) A DECLINE OF 2.3 PERCENT IN CONSUMER EXPENDITURE. AND 2.0 PERCENT IN GOVERNMENT EXPENDITURE.

THE FOLLOWING TABLE SUMMARIZES THE MOST RECENT INDICES:

	1970 EQUALS 100			
	EXPENDITURE	INCOME	OUTPUT	AVERAGE
1976 I	111.0	108.6	108.1	109.2
II	108.4	108.9	107.7	108.3
III	109.3	108.2	107.6	108.4

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IV	111.5	108.7	109.0	109.7
1977 I	110.2	109.7	109.8	109.9

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14. EXCHANGE RATE AND GOLD EFFECTIVE

EXCHANGE RATE

MFANGE (DEC. 1971 GOLD

DATE	RATE (\$	EQUALS 100)	(\$)
6/15	1.7198	61.6	139-1/8
6/16	1.7193	61.5	139-5/8
6/17	1.7196	61.6	139-1/8

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6/20	1.7197	61.6	139-7/8
6/21	1.7196	61.6	141-1/8

CHANGE 6/14-6/21 UP 0.0005 UP 0.1 UP 2-1/2

L5. FORWARD DISCOUNT ON STERLING

DATE	1 MONTH	3 MONTHS	6 MONTHS
6/15	0.60	1.90	3.79
6/16	0.58	1.88	3.87
6/17	0.50	1.72	3.71
6/20	0.40	1.72	3.51
6/21	0.46	1.63	3.53

CHANGE 6/14-6/21 NAR 0.11 NAR 0.17 NAR 0.12

(ALL FIGURES IN CENTS)

16. EURODOLLAR INTEREST RATES

DATE	1 MONTH	3 MONTHS	6 MONTHS
6/15	5-1/8	5-1/2	5-7/8
6/16	5-1/2	5-3/4	6-1/8
6/17	5-1/2	5-3/4	6-1/8
6/20	5-3/4	5-3/4	6-1/4
6/21	5-1/2	5-7/8	6-1/8

CHANGE 6/14-6/21 UNCHANGED UP 1/8 DOWN 1/8

17. THREE-MONTH LONDON INTERBANK - EURODOLLAR INTEREST

RATE DIFFERENTIAL

DATE	
6/15	2-1/4
6/16	2-1/16
6/17	2-3/32
6/20	2-1/8
6/21	2-1/32

CHANGE 6/14-6/21 WIDENED 1/32

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18. STERLING CERTIFICATES OF DEPOSIT

DATE	1 MONTH	3 MONTHS	6 MONTHS
6/15	7-3/16	7-11/16	8-11/16
6/16	7-3/16	7-3/4	8-3/4
6/17	7-7/32	7-3/4	8-23/32
6/20	7-3/16	7-11/16	8-11/16
6/21	7-7/32	7-3/4	8-43/64

CHANGE 6/14-6/21 DOWN 1/32 DOWN 1/32 DOWN L/64

19. THE MINIMUM LENDING RATE WAS UNCHANGED AT 8 PERCENT.
THE AVERAGE TREASURY BILL RATE ROSE BY 0.0095 PERCENT TO
7.4525 PERCENT AT FRIDAY'S TREASURY BILL AUCTION AS
591.14 MILLION POUNDS IN BIDS WERE RECEIVED FOR THE 300
MILLION POUNDS OFFERED. THIS WEEK 400 MILLION POUNDS IN
BILLS WILL BE ON OFFER AS 500 MILLION POUNDS MATURE.

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Disposition Approved on Date:
Disposition Case Number: n/a
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Line Count: 518
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Litigation History: Hold (001 Tobacco) added on 4/16/2009 3:39:07 PM by WASHDCMcGoldRJ, Hold (001 Tobacco) removed on 4/16/2009 3:45:04 PM by WASHDCMcGoldRJ (Litigation Hold Lifted)
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